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June 23, 2005

Chairman Jeff Hatch-Miller
Commissioner Marc Spitzer
Commissioner Mike Gleason
Commissioner Kris Mayes

Re: Environmental Portfolio Standard, Docket No. RE-00000C-05-0030

Dear Colleagues:

In the course of our discussions at the Special Open Meeting held on June 2 and 3, 2005, I expressed my concerns regarding various aspects of the proposed EPS Rules. The purpose of this letter is to elaborate on those concerns and to identify those issues that I feel need additional discussion.

Funding

The most pressing concern that I have with the funding under the proposed Rules is the degree to which small business owners will be impacted by the increase in the surcharge cap from \$13 to \$75 per month. You may recall that when the current incarnation of the Rules was adopted, it was my amendment that changed the surcharge cap for small businesses to \$13 per month instead of the \$39 per month cap imposed on larger non-residential customers. The justification for my position then was that while the large commercial customers of Arizona could easily afford an extra \$39 per month, it would impose too great a burden on local barber shops, restaurants, and every other small, family-owned business. The grounds for my prior conclusion are even more valid when applied to the proposed Rules – if \$39 a month was too great a burden four years ago, then \$75 a month surely is today.

Another issue that concerns me is the fact that under the proposed and current Rules, the entire burden of funding the EPS falls directly upon the ratepayers, be they businesses, school districts, municipalities, towns, or residential. A more equitable distribution of the costs of complying with the EPS could be accomplished by utility investment. Another potential solution lies in the proposed requirement that the monies collected through the EPS surcharge or adjustment mechanism be used only to pay for the "above market costs" of renewable electricity or renewable generation. The definitions of the terms "above market costs" and "market cost of comparative conventional generation" are not found in the proposed Rules. There was some discussion on this issue at the Open Meeting, but this is a matter that warrants further examination.

Penalties

Although there are no explicit penalties in the Rules, the Commission can still impose penalties for non-compliance under Article 15 §19 of the Arizona Constitution. Any penalties recovered would be deposited into the state's general fund. While the possibility of the imposition of sanctions may provide some incentive for utilities to comply with the Rules, so long as the

penalties are greater than the cost of compliance, depositing money into the general fund does little else to promote the development of renewable energy in Arizona.

There is a provision in the proposed Rules that allows utilities to request a waiver in the event that they fail to meet the EPS requirement for a given year. The provision further states that the Commission, upon granting that waiver, may add the unmet kWh requirement from the given year to the EPS requirement for the following year. I would like to discuss the possibility of also providing utilities with the option of making a voluntary payment which would be used for the development of renewable energy sources. The amount of the payment would be based on the unmet kWh requirement.

Independent Administration

While this issue was discussed at the Open Meeting, the matter deserves further exploration. This option does hold some appeal, but there are many unanswered questions regarding the costs and benefits of independent administration. How much do the utilities currently spend on administering the EPS? Will having an independent administrator cost significantly more? Could an independent administrator achieve better results for the same, a slightly higher, or possible lower cost? Do any other states have independent administration of their EPS programs? Have they been successful? Are there any conflicts of interest present for the utilities that could be eliminated by having an independent administrator? How would the utilities be held responsible for their compliance with the EPS if the program were administered by an independent party? These issues and others merit a thorough vetting before the Commission prior to any commitment to such a proposal.

Net Metering/Interconnection Standards

I understand that these issues will be addressed in the Distributed Generation workshops. My concern is the timeframe in which these issues are to be resolved. Significant lag time between the implementation of the new EPS rules and the implementation of a uniform standard for interconnection and net metering may result in additional delays for compliance with the new Rules.

Extra Credit Multipliers

Removal of the multipliers from the Rules in order to eliminate distortion of the portfolio caused by "phantom" kilowatt hours seems appropriate. However, if the in-state requirement is eliminated as well, it may also be appropriate to have a multiplier that applies only to renewable energy generated within the state of Arizona, regardless of the technology used. While elimination of the multipliers will simplify the Rules and level the playing field, there are other issues that are interrelated. For example, some of the benefits of local renewable energy projects, such as improved air quality, may not be realized in Arizona if the majority of renewable energy resources are located elsewhere. How to encourage utilities to invest in renewables here in Arizona should be discussed further.

Set Asides

The EPS has historically had a strong solar electric requirement. Eliminating the solar set-aside in conjunction with the elimination of the extra credit multipliers would reverse the last five years of policy established by the Commission. Stability of policy is vital to the establishment of a robust market. Fairness dictates that for businesses to be able to rely on the Rules, those Rules must be consistent. Without a resolute policy from this Commission on renewable

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energy, the development of a market for alternative sources of energy in this state becomes increasingly uncertain.

While I am optimistic that we that will strengthen the EPS and continue on the path to decreased dependence on fossil fuels, increased reliability, and cleaner air for Arizona, I am concerned that the proposed Rules may lose their focus on one of the primary goals set out by the current EPS - the cultivation of solar resources in this state.

If the proposed Rules are eviscerated to the point that they no longer hold any semblance to the ones currently in place, then I would prefer to remain with the status quo and leave the Rules as they are. Do not assume that because of my strong environmental record that I will vote to approve any new package of Rules bearing the title EPS.

Sincerely,

A handwritten signature in cursive script, reading "William A. Mundell".

William A. Mundell, Commissioner
Arizona Corporation Commission

cc: Brian McNeil
Ernest Johnson
Chris Kempley
Lyn Farmer
Heather Murphy
Docket Control